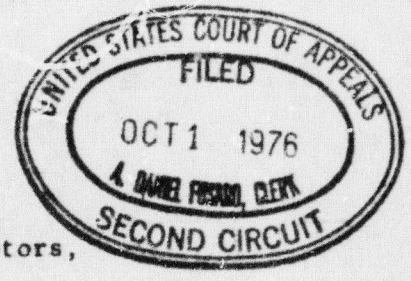
United States Court of Appeals

for the Second Circuit

BRIEF FOR APPELLEE

76-5034

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT



In re

INTERSTATE STORES, INC., et al.,

Debtors,

IRVING SULMEYER, as Receiver for the Estate of ESGRO, INC., a Debtor in Chapter XI,

Plaintiff-Respondent-Appellant,

v.

JOSEPH R. CROWLEY and HERBERT B. SIEGEL, as Reorganization Trustees for WHITE FRONT STORES, INC., et al.,

Defendants-Appellants-Appellees.

Appeal from the United States District Court for the Southern District of New York

BRIEF OF THE SECURITIES AND EXCHANGE COMMISSION, APPELLEE

DAVID FERBER
Solicitor

IRVING H. PICARD
Assistant General Counsel

Securities and Exchange Commission
Washington, D.C. 20549

MERYL E. WIENER
Attorney
New York Regional Office
Securities and Exchange Commission
26 Federal Plaza
New York, New York 10007

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UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 76-5034

In re

INTERSTATE STORES, INC., et al.,

Debtors,

IRVING SULMEYER, as Receiver for
The Estate of ESGRO, INC., a
Debtor in Chapter XI,

Plaintiff-Respondent-Appellant,

v.

JOSEPH R. CROWLEY and HERBERT B.
SIEGEL, as Reorganization Trustees
for WHITE FRONT STORES, INC., et al.,

Defendants-Appellants-Appellees.

Appeal from the United States District Court for the
Southern District of New York

BRIEF OF THE SECURITIES AND EXCHANGE COMMISSION, APPELLEE

COUNTERSTATEMENT OF THE ISSUE PRESENTED

Whether the district judge in a reorganization proceeding under Chapter X of the Bankruptcy Act abused his discretion by revoking his reference to a bankruptcy judge with respect to the determination of a major claim against the estate, and, in the interest of resolving the claim expeditiously in order to facilitate the reorganization, setting the matter down for trial

before him at a date at least six weeks earlier than when the claim might otherwise be tried, which would be in a state court.

COUNTERSTATEMENT OF THE CASE

This is an appeal in the proceeding for the reorganization under Chapter X of the Bankruptcy Act, 11 U.S.C. 501, et seq., of Interstate Stores, Inc., et al. Appellant, Irving Sulmeyer, as the receiver of Esgro, Inc., a debtor whose plan of arrangement under Chapter XI of the Bankruptcy Act, 15 U.S.C. 701, et seq., was recently confirmed (C.D. Cal., No. 73-02510), appeals from an order (A 503-506),[1/] entered on September 1, 1976, by the Honorable John M. Cannella of the United States District Court for the Southern District of New York. That order (1) vacated his reference to a bankruptcy judge with respect to the Esgro claim (A 504); (2) directed that discovery as to that claim be completed by September 27, 1976, and that a stipulation of the parties as to the issues to be tried and the facts involved be filed by October 12, 1976 (A 504-506); and (3) determined that the trustees' objection to the claim be tried before him commencing on October 18, 1976 (A 506). The Securities and Exchange Commission is a party to the reorganization proceeding in the district court, pursuant to Section 208 of Chapter X, 11 U.S.C. 608, and is an appellee on this appeal.[2/]

1/ "A ___" refers to the pages in the joint appendix filed in this appeal.

2/ While the Commission has no right to appeal under that section, as a party to the proceeding the Comminssion is a party to appeals brought by others. See, e.g., In re Imperial '400' National, Inc., 432 F. 2d 232, 234 (C.A. 3, 1970); In re American National Realty Trust, 426 F. 2d 1059, 1066 (C.A. 7, 1970); Ashbach v. Kirtley, 289 F. 2d 159, 162 (C.A. 8, 1961); Scribner & Miller v. Conway, 238 F. 2d 905, 906 (C.A. 2, 1956).

The bankruptcy judge had denied the request of the Chapter X trustees, which the Commission had supported (A 278-283, A 285), to set a hearing for September 15, 1976, on their application to expunge the unsecured claim of $38,758,972 filed on behalf of Esgro in the reorganization proceeding (A 482, A 485, A 6-7).[3/] The bankruptcy judge also noted that a trial date of November 29, 1976, had been set on this matter in a California state court (A 484) in which Esgro had originally filed the same claim as a cross-claim to an action instituted by a subsidiary of Interstate, White Front Stores, Inc., which is also a debtor in this reorganization proceeding. He further stated that modifying the automatic stay under Chapter X Rule 10-601 to permit the prosecution of the claim in the California court would neither prejudice nor harm the trustees and would be "in the interests of justice and convenience of the parties and potential witnesses" (A 485).

The trustees filed a notice of appeal with the district court (A 487-488), pursuant to Bankruptcy Rule 801, made applicable to Chapter X proceedings by Chapter X Rule 10-801, from the bankruptcy judge's order. The district judge set aside the bankruptcy judge's order (A 503). The former noted that the latter had denied the trustees' application and permitted the claim to proceed to trial in California based "primarily on the presently-congested condition of" the bankruptcy court's calendar (A 503). Recognizing that there might be some "slight inconvenience to

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3/ This claim is alleged by Esgro to arise out of the partial cancellation of a licensing and operating agreement between it and certain subsidiaries of Interstate, including White Front Stores, Inc., which are also debtors in this reorganization (A 3-6). Although the stores in question are not in New York, one of the trustees testified (A 151) that White Front's files relating to the Esgro claim are in New York.

the claimant in litigating its claim" in New York (A 504), the district judge found that because of "the magnitude of the Esgro claim, the crucial stage of the reorganization proceedings that has now been reached, [and] the common interest of all the parties in an expeditious" resolution of the claim (A 503-504), "a minor delay at this juncture would place an undue burden on" the reorganization (A 504). Noting that his own calendar would allow him to hear the trustees' objection to the Esgro claim some six weeks before the date available in the California court, he vacated the reference to the bankruptcy judge with respect to this claim and set it down for trial before him commencing on October 18, 1976 (A 504-506).

ARGUMENT

THE DISTRICT JUDGE DID NOT ABUSE HIS DISCRETION IN REVOKING THE REFERENCE TO A BANKRUPTCY JUDGE AND SETTING THE MATTER FOR TRIAL AT THE EARLIEST DATE ON HIS CALENDAR.

Section 196 of Chapter X, 11 U.S.C. 596, provides in pertinent part that objections to any claim "shall be heard and summarily determined by the court." The purpose of the court's exclusive jurisdiction over claims against the debtor, inter alia, is to avoid a situation where, as would be the case if the bankruptcy judge's order here were permitted to stand, litigation in another court might delay the reorganization proceeding.[4/]

Chapter X Rule 10-103(b) provides that a district judge "may, at any time, withdraw a case either in whole or in part from a referee and . . . act himself . . . ."[5/] In fact, in this case an order had been entered on

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4/ Cf. In re Stanndco Developers, Inc., 534 F. 2d 1050, 1052, 1055 (C.A. 2, 1976).

5/ See In re Press Printers & Publishers, Inc., 12 F. 2d 660, 664-665 (C.A. 3, 1926), certiorari denied, 276 U.S. 633 (1928).

August 14, 1975, modifying the prior orders of reference to make it clear that the district judge was reserving his jurisdiction over these reorganization proceedings.[6/]

One of the trustees testified on May 21, 1976, that the total amount of claims filed in the Interstate proceeding approximated $302,000,000 (A 142-143), which at that time had already been reduced by about $80,000,000 (A 143, A 169). In his opinion, the amount of valid claims will be approximately $150,000 (A 144, A 170). The Esgro claim amounts to about $38,700,000 of the approximately $70,000,000 of pending disputed claims (A 144), or about 55%. The trustee also testified that operations were profitable, having earned about $19,450,000 in the fiscal year ended February 1, 1976, and about $13,000,000 in the previous fiscal year (A 166-167). Additionally, approximately $56,000,000 to $57,000,000 excess cash, i.e., funds not needed for every day business operations, had been accumulated (A 164-165, A 170-171). Thus, although Interstate is ripe for reorganization and "the trustees have been working internally with respect

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6/ That order recited that, inter alia, a copy of all proposed orders should be shown to the district judge prior to their entry by the bankruptcy judge and that the district judge reserved

> "the right and jurisdiction to make, from time to time, and at any time, such orders amplifying, extending, limiting or otherwise modifying this order as the court may deem just and proper."

A copy of that order is attached as Exhibit C to the Supplemental Affidavit of Martin I. Shelton in Support of Motion To Dismiss Appeal, verified September 27, 1976, and filed in this appeal.

to the formulation of the plan [of reorganization]" (A 150, A 171-172), the trustee stated that in his view it would be difficult to formulate a realistic and feasible plan without a determination of a claim as large as that filed by Esgro (A 150-151, A 172-173).

As the district judge found, in the present posture of the Interstate reorganization, an early resolution by him of a claim as large as that filed by Esgro is preferable to permitting a trial to commence six weeks later in a California state court. The resolution of a claim of almost $39,000,000 could, for example, materially affect the solvency of Interstate and the continuing participation of thousands of public investors in this reorganization.[7/]

Under these circumstances, we believe a reviewing court should look to whether the district judge abused his discretion, not to whether the bankruptcy judge was "clearly erroneous," the test in Bankruptcy Rule 810. While that test is applicable in most situations, it cannot be here, since under no circumstances would the bankruptcy judge have been able to exercise a discretion comparable to that of the district judge; that is, to have the case set for trial on the district judge's calendar.

7/ One of the trustees testified that in his opinion Interstate would be solvent if only $150,000,000 of claims are allowed and that it would be insolvent if the allowed claims are $220,000,000 (A 147-148).

CONCLUSION

For the foregoing reasons, the order of the district court should be affirmed.

Respectfully submitted,

DAVID FERBER
Solicitor to the Commission

IRVING H. PICARD
Assistant General Counsel

Securities and Exchange Commission
Washington, D.C. 20549
212-755-1238

MERYL E. WIENER
Attorney
New York Regional Office
Securities and Exchange Commission
26 Federal Plaza
New York, New York 10007
212-264-4059

September 1976.

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

OFFICE OF THE
GENERAL COUNSEL

September 30, 1976

A. Daniel Fusaro, Esquire
Clerk, United States Court of
Appeals for the Second Circuit
U. S. Courthouse
Foley Square
New York, New York 10007

Re: In re Interstate Department Stores, Inc.; Sulmeyer v. Crowley and Siegel, C.A. 2, No. 76-5034

Dear Mr. Fusaro:

Enclosed for filing with the Court are ten copies of the BRIEF OF THE SECURITIES AND EXCHANGE COMMISSION, Appellee, in the above-captioned appeal.

I have caused copies of this brief to be served on counsel noted below.

Sincerely,

Irving H. Picard

Irving H. Picard
Assistant General Counsel

Enclosures

cc: Shea, Gould, Climenko & Casey
Weil, Gotshal & Manges
Zalkin, Rodin & Goodman